

# How Top-Performing Dealers Prepare for a Down Cycle

**F**arming and the farm equipment business are and always have been cyclical businesses. That's sometimes easy to forget, especially coming off a few really good years like we are now. But the cycle will turn down and the only question is when.

For big equipment, some analysts are forecasting a downturn as early as mid- to late- 2009. Others say equipment sales will slow in early 2010. Some believe the cycle has already turned. According to the Assn. of Equipment Manufacturers, March 2009 was the first month since January 2007 where sales of large tractors and combines fell compared to the same period of the previous year. Dealers selling livestock and outdoor power equipment have already experienced sharply lower sales for the past year.

It's never too early to begin anticipating a change in business conditions. With the proper preparation and early action, you can adjust in an orderly manner and actually benefit when the cycle turns back up again. In fact, the earlier you anticipate a change — up or down — the better. Too often, dealers wait too long to take necessary actions to protect their business in a down cycle.

Your actions are basic and limited: either reduce expenses, or do what's necessary to maintain gross profits, or a combination of these two.

We emphasize that the second option should be stated as maintaining gross profits and not maintaining revenue or sales. From experience with previous down cycles, we know that it is possible to maintain gross profit even if total revenues decline with lower new or used equipment demand.

Reducing expenses is the usual and easiest option to take. The objective is to plan for expenses that match declining gross profits. You should take the view that all expenses are variable with the exception of some related

to occupancy, like mortgages and the lease and rental of buildings. It's possible to reduce all other expenses.

We stress this view of variable expenses because many times managers wait too long to react and are forced to make deep cuts that are highly disruptive to the business. The reasons for waiting can be fear of laying off employees or denial of the situation or not knowing which action to take first. Viewing all expenses as variable means that you broaden the variety of actions available to you.

Following are suggested actions to reduce personnel, operations and interest expenses.

**Personnel Expenses.** Reduce salary for key managers, furlough hourly employees, lay off, suspend some benefits like 401(k) matches, eliminate overtime — unless incremental profits exceeds costs.

**Operations Expense.** Maximize recovery charges for mileage, diagnostic fees and transport. In our audits, we find that these fees are appropriate in most cases, but are only charged 30-40% of the time.

If only from the standpoint of out-of-pocket costs, charging back the expenses involved in picking up customer equipment and bringing it back to the shop is reasonable. The same holds true for applying costs when delivering a technician to a customer's work site, thereby improving the speed of getting their equipment back up and running.

These actions may be controversial because of your dealership's past practices or those of your competition. But if you are in a survival mode, you need to consider actions such as these that are considered normal in other industries.

**Interest Expense.** First learn to operate with lower inventory (e.g. more pre-sells). Refinance debt if lower

## Productivity Benchmarks of Top Performing Dealers

Shop Productivity = 85%	Billed Hours (customer, internal and warranty) vs. total paid hours. Benchmark for department, not each technician; experienced techs should have a higher benchmark, and newer technicians may have a lower benchmark — wages rates will also be different
Sales People = \$20,000 Gross Profit Per Month	Applies to gross profit on new and used wholegoods, with adjustments for benefits. If sales people are on commission with base salary or draw, combine total earnings to calculate gross profit.
Parts People = \$50,000 Revenue Per Person	Including parts manager in the department head count
Revenue Producers = 75%	Headcount of 75% revenue producing staff and 25% overhead or support staff.

rates are available. Move to bank financing vs. OEM. (This is sometimes necessary as captive financing is reduced or eliminated.) Sell financed inventory assets (new, used or rental) that are still collateralized to relieve the debt. And be sure that you pay the debt down before you use any proceeds for other liabilities when you sell these units. Reduce A/R levels through use of credit cards or manufacturer credit programs (e.g. Farm Plan, etc.)

## Maintain Gross Profits

The second choice is to maintain gross profits, not necessarily sales. Although this requires more creativity and change, we encourage this choice before reducing expenses. Maintaining a budgeted level of profits and cash flow is harder to do but is less disruptive and can mean a better situation when the up-cycle begins. As with expenses, you should anticipate the changes necessary.

Here are some examples for maintaining gross profits in the areas of revenue mix, focused sales training and sales management.

**Improve Revenue Mix.** Increase your parts and service revenues. Take a hard look at your “absorption level” and make sure that you maintain this in both up or down cycles! Absorption is basically the total profit from parts, service and short-term rental business, which if your sales mix is strong enough in the aftermarket business, will cover or “absorb” all the expenses in the dealership. If wholegoods sales are paid on commission, then when sales are down, personnel is down, and when sales go up personnel goes up. This will not impact “absorption” if the sales department is totally scalable to volume.

**Focused Sales Training.** This is a must for all revenue producers, not just sales people. It needs to include

service technicians, parts counter people, and those working with rentals.

**Managing Suppliers.** Many manufacturers are looking for good distribution and support. With product lines the right financial terms from these suppliers (e.g. asset carry, margins, etc.), additional can be a good way to maintain gross profits.

In other cases, you might also want to consider reducing the number of vendors you work with. And just as your customers are asking for concessions, you need to do the same with your suppliers.

The goal is good asset management and providing a product that satisfies your customers’ needs with a balanced investment from you.

**Sales Management.** Require specific sales strategies from sales people for all A & B accounts and assign target accounts to management. Also, conduct more customer seminars so you and the salesmen are ‘hearing the voice of the customer.’

## Know Your Banker

Finally, because cash flow is so important during a down cycle, support from your bank is vital. Don’t forget to educate your banker. He may not completely understand the cyclical and seasonal nature of the ag business. Given the changes and turmoil in the banking system, communication with your current banker and building relationships with other bankers and sources of funding has never been more important.

For the same reasons you bring in technical specialists from your equipment suppliers to train your service staff, you might consider using a consultant or ag industry expert to help “educate” your banker.



## Top Performing Dealers

... think 3 to 6 months in advance. Now is time to think about the down cycle.

... if it’s necessary to lay people off, don’t lay off the newest people. They have clear productivity benchmarks and rank people who are the most productive and contributing the most to the organization.

... look at best practices from other industries. Other equipment industries consider delivery trucks and drivers as a revenue department. If you own your own lowboys, you should at least break even or better yet make money in transporting equipment.

... consider outsourcing transportation needs. Not only will it free up cash, it will also encourage you to bill the customer when you receive the invoice from the delivery/transport company.

... actively manage receivables with progress payments, credit cards on file, thoroughly review credit applications and establish call patterns.

... train parts people on counter and telephone techniques to increase add-on and related sales.

... train field service technicians in selling skills for increasing add-on service work.